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TO RUEHC/SECSTATE WASHDC 6549
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RUEHBK/AMEMBASSY BANGKOK 3800
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RUEHKO/AMEMBASSY TOKYO 9017
RUEHML/AMEMBASSY MANILA 0129
RUEHJA/AMEMBASSY JAKARTA 4122
RUEHKL/AMEMBASSY KUALA LUMPUR 3802
RUEHHI/AMEMBASSY HANOI 3374
RUEHBY/AMEMBASSY CANBERRA 4580
RUEHWL/AMEMBASSY WELLINGTON 1854
RUEHHK/AMCONSUL HONG KONG 8430
RUEHGH/AMCONSUL SHANGHAI 1313
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USTR FOR ALTBACH AND STRATFORD
USDOC FOR 3132/USFCS/OIO/EAP
TREASURY FOR OASIA/TTYANG
TREASURY ALSO PASS TO FEDERAL RESERVE/BOARD OF
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SUBJECT: Big Taiwan State-owned Banks to Merge

REF: (A) TAIPEI 336

¶1. SUMMARY: Taiwan announced a three-year plan to merge the operations of the three largest state-owned banks into one financial holding company. The world ranking of the new firm's banking unit will move up to 89th, and its market share in Taiwan will increase to 18%, well ahead of the next largest bank's share of less than 10%. The plan is a step forward, but it will not reduce the public sector's control of the financial sector. One wonders if this new entity will keep its world ranking for long if it remains a state-owned enterprise. END SUMMARY.

Bank Consolidation Plan Gets the Green Light

¶2. On August 15, the Executive Yuan formally approved a three-stage financial consolidation plan submitted by the Ministry of Finance (MOF). The plan calls for the MOF to set up by the end of this year a new state-owned entity called Taiwan Financial Holding Company (TFHC), which will comprise three state-owned banks - Export-Import Bank of China (EIB), Land Bank of Taiwan (LBT), and Bank of Taiwan (BOT). In July, BOT had already merged with another state-owned bank, Central Trust of China (CTC) (reftel). As part of the reorganization, TFHC will set up two subsidiaries, one transformed from CTC's life insurance department and the other a merged CTC and BOT securities operation. The three banks, however, would initially be managed independently.

¶3. Prior to the end of 2009, however, BOT will merge with EIB, with the new entity still called BOT. EIB's insurance department will be split off and merged into the TFHC's insurance subsidiary. LBT's securities department will merge into TFHC's new securities firm. By the end of 2010, the enlarged BOT will merge with LBT, with the new entity's name remaining BOT.

¶4. As part of the plan, the MOF guaranteed the 14,200 bank employees there would be no layoffs for at least three years. These employees have seen themselves as civil servants, but after the reorganization, TFHC operations will no longer be regulated by the budget, and civil service rules and regulations will no longer apply. Salary caps will be removed for top managers for example. Government bureaucrats are hoping that the new entity will operate more like a private company.

One of the World's 100 Largest Banks

¶5. The MOF projects that after the merger, TFHC's new banking entity will, in terms of assets, be ranked 89th in the world. This puts it larger than Singapore's United Overseas Bank (ranked 102nd), but still smaller than South Korea's Shinhan Bank (ranked 82nd). The new banking entity's assets will increase to US\$158.8 billion, and it will have 308 branches, including 16 overseas. Its market share in terms of loans and deposits will rise to 19%, far higher than any other bank in Taiwan, the next largest having market share of below 10%.

Is Bigger Better?

¶6. The MOF asserts the planned merger will reduce costs and increase efficiency. The firms will also bring different strengths to the new bank. CTC, prior to July, was Taiwan's sole insurance provider to public employees and the major public procurement contractor. BOT is the leader in corporate banking and foreign exchange services, and LBT is the largest in the mortgage, real estate trust, and securitization service supplier. EIB specializes in financial services for overseas trade and investment. The merged

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institution should continue to dominate all of these sectors.

Or Just Bigger?

¶7. Some financial observers in Taiwan have expressed concern that TFHC will become a new financial giant that banks will have difficulty competing with. One analyst of a foreign bank disagreed, however, noting that he expected the larger state-owned entity to be just as inefficient as the banks it absorbed.

COMMENT

¶8. This plan is a political compromise and it shows. By not privatizing the institutions and guaranteeing no layoffs, much of the political opposition was removed, allowing the consolidation to move forward. It may also, however, have removed the chance for the new bank to compete on an equal footing with its rivals. It will indeed be bigger, but it is unlikely to outmaneuver nimble non-government competitors who will also be seeking to serve an increasingly discerning market.

WANG